Liquidity letter
n°119 I 19 Sept 2024

Fed: time for easing

The Fed strikes a blow

The Federal Reserve announced a 50 bp rate cut on Wednesday evening, to 4.75%-5%, the first since the 2020 pandemic.

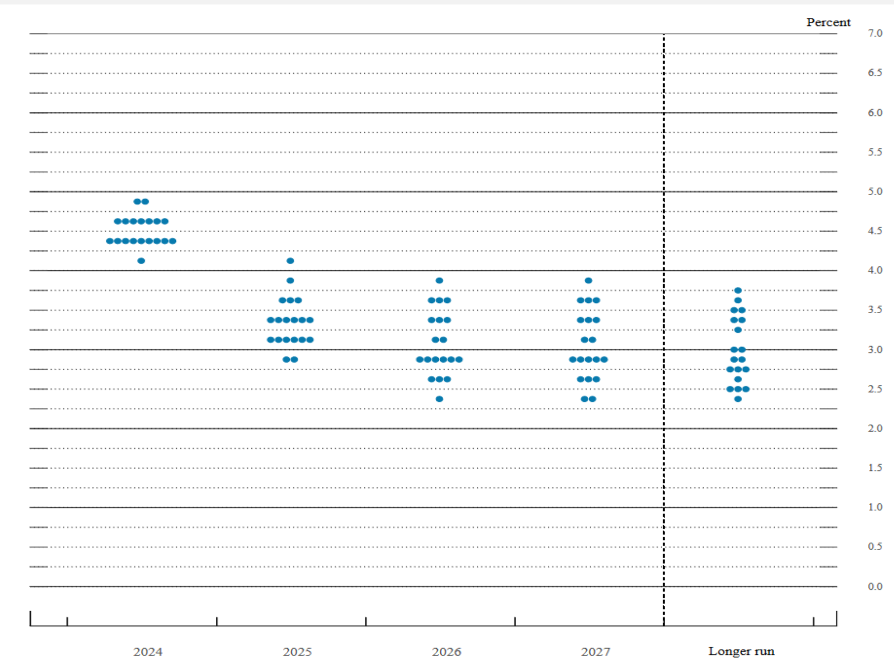
The decision was not unanimous, as Governor Michelle Bowman had voted for a cut of just 25 bp. The cut was expected, but only uncertainty remained as to its magnitude.

In June, the Fed thought it would cut rates only once in 2024, by 25 bp. But since then, the job market has slowed more than expected, and fears of recession have resurfaced. This rate cut should restore purchasing power to American households, who have been squeezed for several years by high inflation and the high cost of credit.

"The Committee has gained greater confidence in the sustainable decline in inflation towards 2%", target level considered healthy for the economy, said the FOMC in its statement. And further rate cuts are on the cards, as Jerome Powell indicated that the 50 bp cut should not be interpreted as a new pace, suggesting instead 25 bp cuts at future meetings.

By lowering rates, the Fed wants to prevent unemployment from rising in turn, while inflation seems to be under control.

Assessment by FOMC members



Source : Federal Reserve

Number of the week

-50 bp

Fed rate cut
(September)

Further rate cuts by the end of 2024

The next step for Fed officials is to determine the pace at which they need to implement rate cuts to achieve a balance between inflation and growth.

At the press conference, Powell said there was no "rush". The dots chart also showed dispersion among Fed officials, not only for this year, but also for 2025.

2 out of 19 members believe that the Fed should keep rates unchanged at these levels until the end of the year, while 7 others expect a single 25 bp cut.

The markets have already priced in the fact that rates will fall further than the Fed expects, reaching 4% to 4.25% by the end of the year, which would imply further significant cuts in the two remaining meetings in 2024.

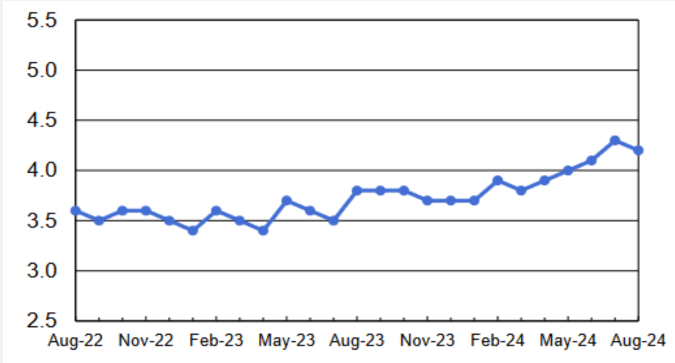
U.S. job market on the decline

In August, the US labor market showed signs of recovery, but with mixed results. Hiring rose modestly, with 142,000 new jobs created, below expectations of around 160,000.

The unemployment rate fell slightly from 4.3% in July to 4.2% in August, marking the first improvement in several months. However, some sectors, notably durable goods manufacturing and retail trade, lost jobs.

Wage growth also showed positive signs, with an increase of 0.4% in August, reinforcing the annual trend of 3.8%.

US unemployment rate (%)

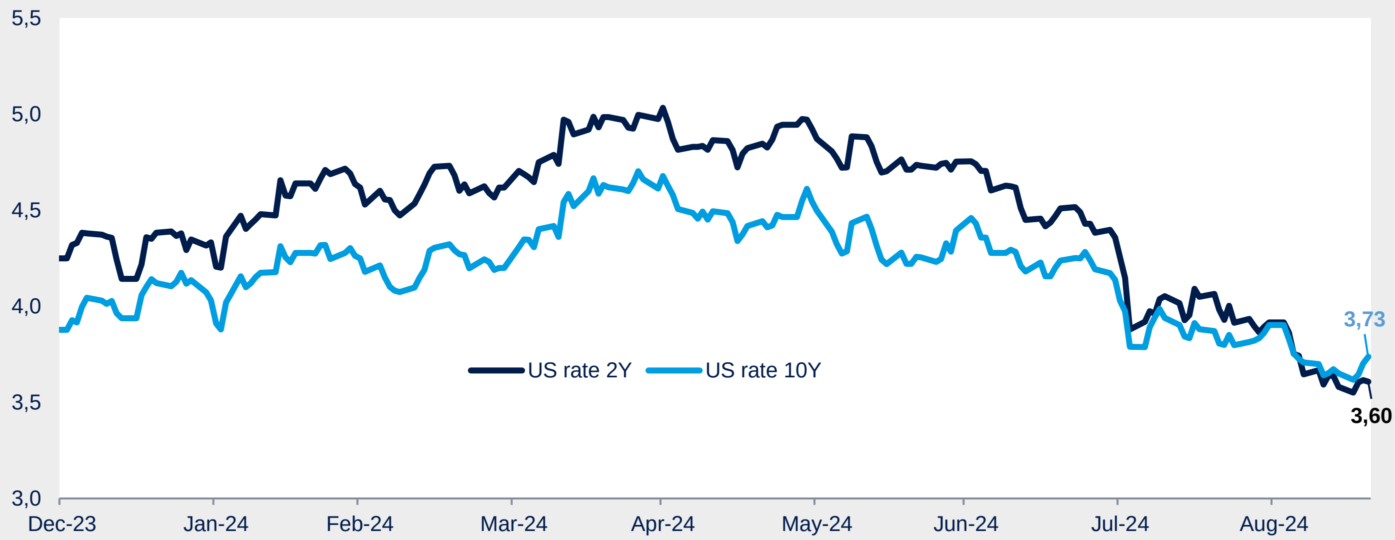


Source : Bureau of Labor Statistics

> *This decision reflects our growing confidence that, with an appropriate recalibration of our policy, the strength of the labor market can be maintained in a context of moderate growth and inflation on a sustained downward trend towards 2%.*
>
> *Jerome Powell, President of the Fed, 18 September 2024*

Market Impact

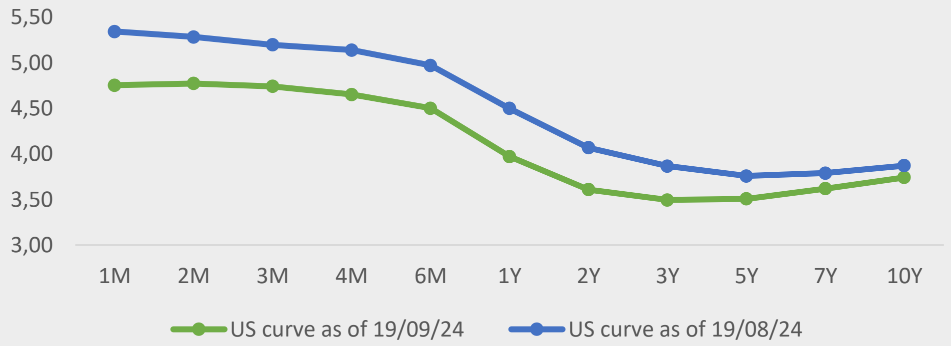
US 2-year and 10-year rates (%)



Following the announcement of the Fed's rate cut, U.S. 2-year and 10-year yields changed little, as the markets had already incorporated the 50-bp cut. Thus, the 2-year rate (sensitive to monetary policy) lost just 3 bp over 1 week, while the 10-year rate rose by 10 bp over the same period.

Source : Amundi, Bloomberg

US yield curve (%)



The US yield curve continues to flatten.

Source : Amundi, Bloomberg

ZEW index collapses in Germany

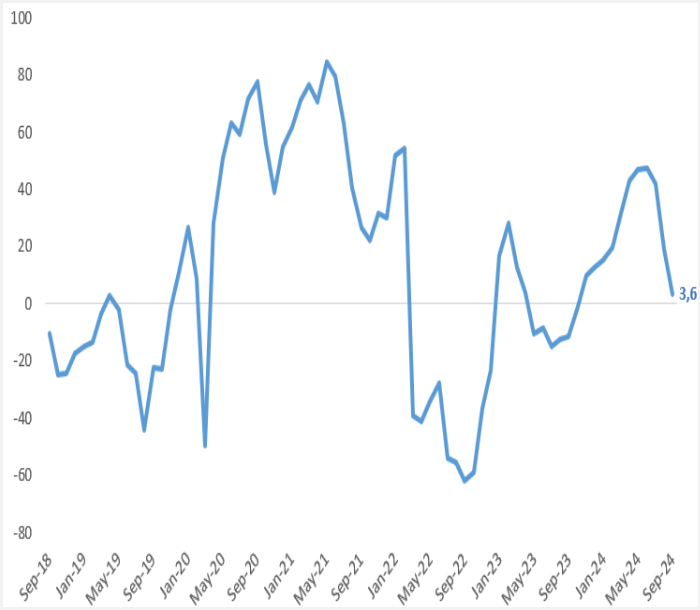
The ZEW index, measuring German investor sentiment on the economic outlook, came in at 3.6 in September, compared with 17.1 expected after 19.2 in August. The economic outlook deteriorated dramatically and unexpectedly in September, signaling a sharp loss of confidence in the eurozone's largest economy.

This decline reflects a worsening economic outlook in Germany, particularly due to concerns about persistent inflation and slowing domestic and foreign demand.

At the same time, the current conditions indicator also plunged, from -77.3 points in August to -84.5 points in September, reflecting an increasingly pessimistic view of economic conditions in the country.

Germany dragged the Eurozone down with it, with the ZEW index dropping to 9.3 points from 17.9 the previous month.

German ZEW index



Source : Amundi, Bloomberg

News

United Kingdom | Final inflation rate at 2.2% (August)

Euro Zone | Final inflation rate at 2.2% (August)

Agenda

23 September I Publication PMI composite index in Euro Zone (Sept)

27 September I Publication inflation rate in France (Sept)

Follow-us